Cash Flow Case Study

Denise Smilie owns a gift shop, Giftz, and has been operating the business for the past 3 years. She is quite busy at present as it is the peak season and increasing numbers of tourists are visiting the shop. It is not September, and Denise plans to close the shop in January, to go on holiday to Australia. Her daughter, Danni, has recently completed a Business Studies course and is keen to help with the business. Although the business is reasonably profitable, Danni is surprised to learn that Denise has not prepared a cash flow forecast. She gathers information in order to prepare a cash flow forecast for the next 4 months. The information is summarized as follows:

1. Cash Sales are forecast to be $8000, $15000, $20000, and $0, for the months of October, November, December and January respectively.
2. Cash payments for purchases are expected to be $9000, $15000, $10000 and $0 for the months of October, November, December and January respectively.
3. Cash payments for expenses such as wages and salaries are budgeted at $500 per month for each month in the period October to January.
4. Cash payments for other overheads related to the shop are expected to amount to $120 per month, payable on the 28th day of each month.
5. Whilst Denise is on holiday in January, repairs to the shop will be carried out, costing $6000, which is payable to the builder on the 28th day of February.

The opening balance as at 1st October is expected to be $3000.

1. Explain what is meant by the term cast flow forecast.
2. Prepare the cash flow forecast for Giftz, showing the closing cash balance as at the end of each month in the budget period, October to January.
3. Explain two ways in which Giftz could overcome potential cash flow difficulties, without raising more capital, thus improving the cash flow of the business.
4. Explain how the cash flow of a business such as Giftzs, differs from its profits.
5. Evaluate the usefulness of preparing a cash flow forecast, for a business such as Giftz.